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BEFORE THE ARIZONA CORPORATION COMMISSION
AZ CORP COMMISSION

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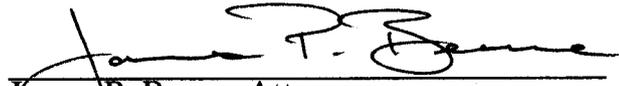
IN THE MATTER OF COMPETITION
IN THE PROVISION OF ELECTRIC
SERVICES THROUGHOUT THE
STATE OF ARIZONA.

DOCKET NO. U-0000-94-165

**NOTICE OF FILING COMMENTS TO THE
COMMISSION STAFF'S DRAFT RULE**

The Residential Utility Consumer Office ("RUCO") hereby provides notice of filing
its Comments to the Commission Staff's draft rule on electric industry restructuring.

RESPECTFULLY SUBMITTED this 12th day of September, 1996.


James P. Beene, Attorney
Residential Utility Consumer Office

AN ORIGINAL AND TEN COPIES of the
foregoing filed this 12th day of
September, 1996 with:

Arizona Corporation Commission
DOCKETED

Docket Control
Arizona Corporation Commission
1200 W. Washington
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SEP 12 1996

DOCKETED BY 

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**Preliminary Comments of
Residential Utility Consumer Office**

on the

**Arizona Corporation Commission Staff's
Proposed Rule on Retail Electric Competition**

September 12, 1996

General Comments

RUCO is concerned that the Staff's "Proposed Rule" is more in the nature of a preliminary draft than a considered set of proposed regulations. The Draft shows many signs of haste and incompleteness.

Moreover, the Draft is premature. It rushes to judgment on a number of policy issues that should first be the subject of due deliberation before the Commission. RUCO urges the Commission to make the appropriate policy decisions following a proper evidentiary proceeding, after which Staff should be directed to develop regulations to implement those policy decisions.

Furthermore, a major issue that needs to be faced by the Commission before regulations are drawn up is whether its own powers under the Arizona constitution and current law are sufficiently broad to allow it to undertake the restructuring of the electric industry without a prior legislative mandate. RUCO frankly doubts that the Commission has the necessary authority to introduce retail electric competition in Arizona, considering the fact that the nature of the utility franchise -- which has hitherto been the legal foundation of the electric industry's organization and regulation in the state -- would be dramatically changed.

Given the short time made available to RUCO and other parties, these comments, like the Draft rule, will unfortunately be preliminary and incomplete.

Definitions

"Stranded Investment" is defined in the draft in a manner that does not take into account various kinds of potentially stranded electric utility costs that are not necessary "investments." These costs could include the costs of purchased power or fuel contracts, regulatory assets, nuclear facility decommissioning costs and waste fuel disposal, etc.

Definitions are needed of power suppliers and electric utilities in the new industry structure. A clear distinction should be drawn between a power supplier (which supplies electricity) a distribution utility (which delivers it). Power suppliers may or may not be generators of electricity (which produce it), which should also be defined. As noted earlier, the rights of the electric (distribution) utility should be clearly described.

Related to the above point, RUCO believes that Staff may intend retail competition to include not only electricity generation and supply, but also distribution. If this is the case, this would be a very different policy position from

that taken by commissions and legislators in other states. It is generally regarded as desirable to allow utilities to keep an exclusive franchise of electricity distribution or delivery in specified territories. Distribution, unlike generation, is still generally regarded as a "natural monopoly" that is most economically provided by a single system in each area. Furthermore, opening up distribution to competition would create a situation in which competitors would select the most profitable customers or areas, leaving others under monopoly control. This would be highly discriminatory, tantamount to "red-lining" areas.

The concept of "buy-through" is a controversial one. Customers will generally prefer to have the right to buy electricity directly from suppliers of their choice, without the utility intervening in the transaction except as distributor responsible for system reliability.

Solar energy and renewable energy resources are not defined. RUCO is generally troubled about the apparent intention of the Draft to develop specific rules covering some energy resources. It would be preferable in a competitive generation market for the Commission to leave issues regarding types of resources in the hands of power producers under the regulation of environmental agencies. (The Commission might still have a role in the area of reliability.)

Filing of Tariffs by Affected Utilities

It would, in RUCO's view, be premature to require utilities to file final tariffs by June 30, 1997. For one thing, the treatment of stranded costs in such tariffs is too important to be resolved finally by that time.

On the other hand, it might not be premature to have preliminary tariffs in place for purposes of retail competition Pilot Programs.

The issue of Pilot Programs is one that needs a determination by the Commission. Earlier, Staff was considering requiring Pilot Programs. RUCO and some other parties have been supportive of that concept. But it is nowhere mentioned in the Draft. Instead of initially opening retail competition under a pilot to 3% or 5% of retail customers, in order to give utilities, marketers, generators, customers and regulators an initial opportunity to test out the structure and functioning of a competitive retail market, the Draft would introduce competition for 20% of customers at one time, by January 1, 1999. This is unnecessarily delayed, and, when it comes, it is a large number of customers for a first phase.

Certificates of Convenience and Necessity

While RUCO supports the regulation of power suppliers to protect consumers and to protect the reliability and integrity of the electric grid, Staff's proposals go further than is necessary and smack of the old kind of regulation that effective competition should render obsolete. For example, the filing of tariffs, description of geographic areas, city approvals, and business plans go further than may be necessary.

Competitive Phases

As noted earlier, the advent of retail competition is unnecessarily delayed. RUCO also believes that the rules for access should be considered very carefully to ensure that all customer classes have the opportunity to participate equally in the competitive market.

A simple requirement that the right to direct retail access shall be phased in for all customer classes in proportion to their sales might be preferable than the Staff's proposals. For example, initial access under a Pilot Program could be for 4% of the load of each major customer class, later 10% or 20%, and so on.

January 1, 2003 -- over six years from today -- is too long for customers to wait for complete retail access.

The "buy-through" and solar energy provisions of the Staff Draft are problematic, and, at least require substantial discussion and review by interested parties.

Competitive Services

This section of the Draft is confusing. In RUCO's opinion, a clear distinction should be drawn between distribution service which is provided by the (distribution) utility -- which might, or might not, also be offering packaged Standard Offer service -- and power generation and supply, which can be offered by registered power suppliers. If they can meet environmental standards and obtain siting permits from appropriate environmental agencies, generation could be on-site ("distributed") or remote (delivered by the distribution utility). There seems to be no need to draw a major distinction between central station and distributed generation.

RUCO does not believe that termination of Standard Offer service should be contemplated in the foreseeable future. If customers can do better, they should be free to reject Standard Offer service and choose alternative suppliers. Standard

Offer service could conceivably dwindle away, although RUCO doubts that will happen. It is much more likely that many types of customers will prefer simple "one-stop" service -- possibly students and other temporary customers, start-up small businesses, low-income or low-use customers, etc.

Recovery of Stranded Investment of Affected Utilities

RUCO mentioned at the outset that "stranded investment" is too narrow a concept and should be broadened to include other types of "stranded costs."

While there are many features of the Staff's relatively detailed treatment of this issue that may well survive careful scrutiny, there are some features that are questionable. For example, the reference to "exit fees" is problematic insofar as it may be anti-competitive to impose such fees on departing customers.

Rather than recover stranded costs (or the portion of them that the Commission determines should be recovered from customers) from only "customers served competitively" it would be preferable to identify all uneconomic or potentially strandable costs and include them (to the extent recoverable) in the rates of *all* distribution customers. Whether they are explicitly identified in bundled rates is a relatively minor point, what matters is that all customers (whether they continue to take Standard Offer service or switch to a competitive supplier) should equally share in costs determined to be recoverable. In this manner, generation prices (whoever the supplier) will be free of stranded costs and will be economic, market-determined prices.

System Benefits Charge

As with stranded cost charges, system benefits charges could be separated out and directly charged to *all* customers, whether or not identified separately in the bill. It should not be controversial to explicitly identify these charges, which will probably be small compared to stranded cost charges.

Solar Portfolio Standard

RUCO is concerned about the policy assumption underlying these provisions, that the Commission should play a major role in determining the types of resources developed in a competitive market. As suggested earlier, decisions about resource types should be left to the market, subject to environmental standards, etc. (Reliability, which affects all customers on the system, is another matter.)

Pooling of Generation and Centralized Dispatch of Generation or Transmission

This portion of the Draft needs to recognize the essential role of the Federal Energy Regulatory Commission, which will continue to have, as it does now, a central role in matters relating to transmission tariffs, open access on the transmission system, pooling arrangements, wholesale competition and other aspects of the structure and functioning of wholesale or bulk-power markets.

In-State Reciprocity

RUCO believes that the legislature may have a role in determining which utilities shall be "affected utilities."

Rates

RUCO believes, as noted earlier, that in a market determined to be competitive, suppliers should not have to file rates with the Commission, or be subject to Commission approval. For example, there should be no provision that would require the Commission to investigate whether rates are below the "marginal cost of providing the service."

Consumer protection laws should, however, be extended to apply to electric service. Moreover, the Commission should be required to make a determination that the supply market is competitive, and intervene in the market to ensure that anti-competitive practices do not arise or, if they do, are penalized and terminated.

Conclusion

RUCO recommends that the Commission establish a phase of the restructuring investigation to take evidence from all parties and reach a considered judgment regarding restructuring *policies*. It should then sponsor appropriate *legislation* as necessary. Finally, it should in due course develop *regulations* that implement the policies as embodied in its policy order and legislation.